



[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-104223-18]

RIN 1545-B052

Ownership Attribution Under Section 958 Including For Purposes of Determining Status as Controlled Foreign Corporation or United States Shareholder

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the modification of section 958(b) of the Internal Revenue Code (“Code”) by the Tax Cuts and Jobs Act, which was enacted on December 22, 2017. The proposed regulations affect United States persons that have ownership interests in or that make or receive payments to or from certain foreign corporations.

DATES: Written or electronic comments and requests for a public hearing must be received by **[INSERT DATE 60 DAYS AFTER PUBLICATION IN THE FEDERAL**

REGISTER].

ADDRESSES: Send electronic submissions via the Federal eRulemaking Portal at www.regulations.gov (indicate IRS and REG-104223-18) by following the online instructions for submitting comments. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The Department of the Treasury (the “Treasury Department”) and the IRS will publish for public availability any comment

received to its public docket, whether submitted electronically or in hard copy. Send hard copy submissions to: CC:PA:LPD:PR (REG-104223-18), Room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044.

Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG-104223-18), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC 20224.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Jorge M. Oben, (202) 317-6934; concerning submissions of comments and requests for a public hearing, Regina Johnson at (202) 317-6901 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

Section 958 provides rules for determining direct, indirect, and constructive stock ownership. Under section 958(a)(1), stock is considered owned by a person if it is owned directly or is owned indirectly through certain foreign entities under section 958(a)(2). Under section 958(b), section 318 applies, with certain modifications, to the extent that the effect is to treat any United States person as a United States shareholder within the meaning of section 951(b) ("U.S. shareholder") of a foreign corporation, to treat a person as a related person within the meaning of section 954(d)(3), to treat the stock of a domestic corporation as owned by a U.S. shareholder of a controlled foreign corporation ("CFC") for purposes of section 956(c)(2), or to treat a foreign corporation as a CFC under section 957.

Section 318 provides rules that attribute the ownership of stock to certain family members, between certain entities and their owners, and to holders of options to

acquire stock. Section 318(a)(1) provides rules attributing stock ownership among members of a family. Section 318(a)(2) provides rules attributing stock ownership from partnerships, estates, trusts, and corporations to partners, beneficiaries, owners, and shareholders (so-called “upward attribution”). Section 318(a)(3) generally attributes stock owned by a person to a partnership, estate, trust, or corporation in which the person has an interest (so-called “downward attribution”). In particular, section 318(a)(3)(A) provides that stock owned, directly or indirectly, by or for a partner or a beneficiary of an estate is considered as owned by the partnership or estate. This provision applies to all partners and beneficiaries without regard to the size of their interest in the partnership or estate. Section 318(a)(3)(B) similarly provides, subject to certain exceptions, that stock owned, directly or indirectly, by or for a beneficiary of a trust (or a person who is considered an owner of a trust) is considered owned by the trust. Section 318(a)(3)(C) provides that stock in one corporation owned, directly or indirectly, by or for a shareholder in a second corporation is considered owned by the second corporation if 50 percent or more in value of the stock in the second corporation is owned, directly or indirectly, by such shareholder.

As in effect before repeal, section 958(b)(4) provided that subparagraphs (A), (B), and (C) of section 318(a)(3) (providing for downward attribution) were not to be applied so as to consider a United States person as owning stock owned by a person who is not a United States person (a “foreign person”). Effective for the last taxable year of foreign corporations beginning before January 1, 2018, and each subsequent year of the foreign corporations, and for the taxable years of U.S. shareholders in which or with which such taxable years of the foreign corporations end, section 958(b)(4) was

repealed by section 14213 of the Tax Cuts and Jobs Act, Pub. L. 115-97 (2017) (the “Act”). As a result of this repeal, stock of a foreign corporation owned by a foreign person can be attributed to a United States person under section 318(a)(3) for purposes of determining whether a United States person is a U.S. shareholder of the foreign corporation and, therefore, whether the foreign corporation is a CFC. In other words, as a result of the repeal of section 958(b)(4), section 958(b) now provides for downward attribution from a foreign person to a United States person in circumstances in which section 958(b), before the Act, did not so provide. As a result, United States persons that were not previously treated as U.S. shareholders may be treated as U.S. shareholders, and foreign corporations that were not previously treated as CFCs may be treated as CFCs.

The legislative history to the Act indicates that the repeal of section 958(b)(4) was intended “to render ineffective certain transactions that are used to [sic] as a means of avoiding the subpart F provisions.” See H.R. Rep. No. 115-466, at 633 (2017) (Conf. Rep.). It further provides:

One such transaction involves effectuating “de-control” of a foreign subsidiary, by taking advantage of the section 958(b)(4) rule that effectively turns off the constructive stock ownership rules of 318(a)(3) when to do otherwise would result in a U.S. person being treated as owning stock owned by a foreign person. Such a transaction converts former CFCs to non-CFCs, despite continuous ownership by U.S. shareholders.

Id. at 633-34.

Explanation of Provisions

I. Changes in Connection with Repeal of Section 958(b)(4)

This notice of proposed rulemaking proposes changes that are generally intended to ensure that the operation of certain rules is consistent with their application before the Act's repeal of section 958(b)(4), as further explained in this Part I. Other guidance that provides relief concerning the effect of the repeal of section 958(b)(4) on the application of subpart F more generally is provided separately.

A. Section 267: Deduction for certain payments to foreign related persons

Section 267(a)(2) provides a matching rule that governs the time at which an otherwise deductible amount owed to a related person may be deducted. Specifically, section 267(a)(2) provides that, in the case of certain interest and expenses paid by the taxpayer to a related person, if an amount is not includible in the payee's gross income until it is paid, the amount generally is not allowable as a deduction to the taxpayer until the amount is includible in the gross income of the payee.

Section 267(a)(3)(A) provides that the Secretary shall by regulations apply the matching principle in section 267(a)(2) in cases in which the payee is a foreign person. Section 1.267(a)-3(b) generally requires a taxpayer to use the cash method of accounting for deductions of amounts owed to a related foreign person. An exemption is provided in §1.267(a)-3(c)(2) for any amount, other than interest, that is income of a related foreign person with respect to which the related foreign person is exempt from U.S. tax on the amount owed pursuant to a treaty obligation of the United States.

Section 841(b) of Pub. L. 108-357 (2004) added section 267(a)(3)(B) to the Code, effective for payments accrued on or after October 22, 2004. Section 267(a)(3)(B)(i) provides that, notwithstanding section 267(a)(3)(A), in the case of any item payable to a CFC, a deduction is allowable to the payor with respect to the amount

for any taxable year before the year in which paid only to the extent that an amount attributable to the item is includible during such prior taxable year in the gross income of a United States person who owns (within the meaning of section 958(a)) stock in such corporation. Section 267(a)(3)(B)(ii) grants the Secretary the authority to issue regulations exempting transactions from section 267(a)(3)(B)(i).

For amounts accrued on or after October 22, 2004, a taxpayer that owes an amount to a CFC cannot rely on the exemption in §1.267(a)-3(c)(2) to generally deduct the amount when accrued, and instead can deduct the amount prior to the year the amount is paid only to the extent that an amount attributable to the item is includible in gross income of a U.S. shareholder that owns (within the meaning of section 958(a)) stock in the CFC. After the repeal of section 958(b)(4), a CFC may not have any U.S. shareholders that own stock within the meaning of section 958(a) (“section 958(a) U.S. shareholders”). Because the repeal of section 958(b)(4) is effective for the last taxable year of foreign corporations beginning before January 1, 2018, and each subsequent taxable year of the foreign corporations, and for the taxable year of U.S. shareholders in which or with which such taxable year of the foreign corporations end, a taxpayer may have, in 2017, deducted an amount accrued in 2017 that, due to the repeal of section 958(b)(4), would no longer be allowable in 2017.

The purpose of the matching principle in section 267(a)(2) is to align the timing of a deduction with the inclusion of the item in income. If an amount is owed to a CFC that has no section 958(a) U.S. shareholders that would include an amount attributable to the item in income, and the CFC is exempt from U.S. tax on the amount owed due to a treaty, it is unnecessary to not allow a taxpayer to take the deduction when the amount

is accrued. Accordingly, the proposed regulations provide that an amount (other than interest) that is income of a related foreign person with respect to which the related foreign person is exempt from U.S. taxation on the amount owed pursuant to a treaty obligation of the United States is exempt from the application of section 267(a)(3)(B)(i) if the related foreign person is a CFC that does not have any section 958(a) U.S. shareholders. Proposed §1.267(a)-3(c)(4).

These proposed regulations also amend §1.267(a)-3(c)(2) and remove the rules currently in §1.267(a)-3(c)(4), in order to reflect the changes to section 267 in Pub. L. 108-357. The Treasury Department and the IRS intend to update other provisions in §1.267(a)-3 to take into account the changes made to section 267(a)(3) by Pub. L. 108-357 in future guidance.

B. Section 332: Liquidation of applicable holding company

Section 332(a) provides a general rule that no gain or loss is recognized on the receipt by a corporation of property distributed in complete liquidation of another corporation. Section 332(d) was enacted to disallow the nonrecognition of gain to a foreign corporation through the complete liquidation of certain domestic holding companies, which could avoid the imposition of withholding tax that would otherwise apply to a section 301 distribution from these holding companies. See H.R. Rep. No. 108-755, at 761-62 (2004) (Conf. Rep.). Section 332(d)(1) provides an exception to sections 332(a) and 331 for certain distributions by domestic corporations to foreign corporations. Section 332(d)(1) results in the recognition by a foreign corporation of income from the liquidation of certain domestic holding companies by treating the liquidating distribution as a distribution under section 301. Specifically, section

332(d)(1) provides that section 301, and not section 332(a) nor 331, applies to a distribution to a foreign corporation in complete liquidation of an applicable holding company (as defined in section 332(d)(2)). Section 332(d)(3) provides that, notwithstanding section 332(d)(1), exchange treatment under section 331 applies if the distributee of a distribution in complete liquidation of an applicable holding company is a CFC. In such a case, the gain on the distribution could be foreign personal holding company income (“FPHCI”) under section 954(c)(1)(B), and before the Act, CFCs generally had U.S. shareholders that would be subject to tax on their pro rata share of such gain under section 951(a).

Section 332(d)(4) grants the Secretary the authority to issue regulations as appropriate to prevent the abuse of section 332(d). The repeal of section 958(b)(4) broadened the application of section 332(d)(3) to foreign corporations that are CFCs because of downward attribution from a foreign person. This result could lead to inappropriate results because any gain recognized on an exchange of stock of an applicable holding company under section 331 by a foreign corporation that is a CFC due to downward attribution from a foreign person could avoid U.S. tax if the CFC does not have U.S. shareholders that have current income inclusions under section 951(a). Therefore, in accordance with the regulatory authority provided in section 332(d)(4), the proposed regulations modify the definition of a CFC (so as to use the definition of a CFC in effect immediately before the repeal of section 958(b)(4)) for purposes of applying section 332(d)(3). See proposed §1.332-8(a). The Treasury Department and the IRS request comments on these proposed changes to the definition of a CFC for the purposes of applying section 332(d)(3).

C. Section 367(a): Triggering events exception for other dispositions or events under §1.367(a)-8(k)(14)

Section 367(a)(1) provides that if, in connection with an exchange described in section 332, 351, 354, 356, or 361, a United States person transfers property to a foreign corporation, the foreign corporation is not treated as a corporation for purposes of determining the extent to which gain is recognized on the transfer. Section 367(a)(1) does not apply, however, to certain transfers of stock or securities of a foreign corporation (including an indirect stock transfer) by a United States person (“U.S. transferor”) if the U.S. transferor enters into a gain recognition agreement (“GRA”) with respect to the transferred stock or securities. See §1.367(a)-3(b)(1). In general, a U.S. transferor subject to a GRA must recognize gain if a triggering event (as defined in §1.367(a)-8(j)) occurs during the term of a GRA. See §1.367(a)-8(j). Section 1.367(a)-8(k) provides several exceptions for certain dispositions that constitute nonrecognition transactions if, immediately after the disposition, the U.S. transferor meets certain requirements. In particular, §1.367(a)-8(k)(14) generally provides that a disposition or other event is not a triggering event if the disposition or other event qualifies as a nonrecognition transaction, and, immediately after the disposition or other event, the U.S. transferor retains a direct or indirect interest in the transferred stock or securities or, as applicable, in substantially all of the assets of the transferred corporation. The rule further provides that if a foreign corporation acquires the transferred stock or securities or, as applicable, substantially all the assets of the transferred corporation, the exception applies only if the U.S. transferor owns at least five percent (applying the attribution rules of section 318, as modified by section 958(b)) of the total voting power and the total value of the outstanding stock of such foreign corporation. This five-

percent ownership condition is intended to limit the application of the general exception to transactions in which the U.S. transferor retains at least a minimal interest in the transferred stock or securities (or substantially all the assets of the transferred corporation). See TD 9446, 74 FR 6952, 6953 (February 11, 2009).

The exception described in the preceding paragraph was added when section 958(b)(4) did not allow for downward attribution from foreign persons. A U.S. transferor that would not have been eligible for the exception because it held a less than five percent interest in the transferred stock or securities (or substantially all the assets of the transferred corporation) could now be eligible for the exception if the U.S. transferor holds at least five percent due to downward attribution of stock owned by a foreign person. A U.S. transferor's constructive ownership interest should not include an interest that is treated as owned as a result of downward attribution from a foreign person as it would inappropriately treat the U.S. transferor as owning an interest it would not have owned under the rules in effect when §1.367(a)-8(k)(14) was added. Therefore, in accordance with the regulatory authority provided in section 367(a), the proposed regulations revise §1.367(a)-8(k)(14) to apply section 958(b) without regard to the repeal of section 958(b)(4). See proposed §1.367(a)-8(k)(14)(ii). The Treasury Department and the IRS request comments on these proposed revisions to §1.367(a)-8(k)(14).

D. Section 672: CFC's ownership of a trust

Section 672(f)(1) generally provides that the grantor trust rules in sections 671 through 679 apply only to the extent they result in income being currently taken into account (either directly or through one or more entities) by a citizen or resident of the

United States or a domestic corporation. To the extent that a trust or a portion thereof is not taxed as a grantor trust, the trust and its beneficiaries are taxable in accordance with the rules of sections 641 through 669. In the case of a foreign nongrantor trust, accumulation distributions are not only taxable to U.S. beneficiaries, but also subject to the “throwback rules” of sections 665 through 668.

Section 672(f)(3)(A) provides special rules, however, for a trust that is treated as owned by a CFC. Except as otherwise provided by regulations, CFCs are treated as domestic corporations for purposes of section 672(f)(1). Section 672(f)(3)(A). Before the repeal of section 958(b)(4), the portion of a trust’s income that was treated as owned by a CFC would generally have been taxable currently to the U.S. shareholders to the extent the trust’s income constituted subpart F income of the CFC.

After the repeal of section 958(b)(4), however, a CFC may have no U.S. shareholders that would be subject to tax on their pro rata share of its subpart F income under section 951(a). A CFC could be formed to facilitate tax-free accumulation of income in a trust for the benefit of United States persons and result in tax-free distributions from the trust to the U.S. beneficiaries. In such a case, none of the income or gain of the grantor trust would be taken into account by U.S. shareholders, despite constituting subpart F income, while distributions of income from the trust to its U.S. beneficiaries would not be subject to tax, and the throwback rules would be avoided entirely.

Therefore, the proposed regulations, in accordance with the regulatory authority provided in section 672(f)(3), provide that the only CFCs taken into account for purposes of section 672(f) are those that are CFCs without regard to downward

attribution from foreign persons. See proposed §1.672(f)-2(a). A reference to foreign personal holding companies in §1.672(f)-2(a) is also deleted, consistent with the repeal of the foreign personal holding company regime by section 413(a) of the American Jobs Creation Act of 2004, Pub. L. 108-357. Id. The Treasury Department and the IRS request comments on these proposed revisions to §1.672(f)-2(a).

E. Section 706: Taxable year of partnership

Section 706 provides rules for determining the taxable year of a partnership and its partners. Section 1.706-1(b)(6)(i) provides that in determining the taxable year of a partnership under section 706(b) and the regulations thereunder, any interest held by a disregarded foreign partner is not taken into account. A foreign partner is a disregarded foreign partner unless the foreign partner is allocated any gross income of the partnership that was effectively connected (or treated as effectively connected) with the conduct of a trade or business within the United States (“effectively connected income”) during the partnership’s taxable year immediately preceding the current taxable year (or, if such partner was not a partner during the partnership’s immediately preceding taxable year, the partnership reasonably believes that the partner will be allocated any such income during the current taxable year) and taxation of that income is not otherwise precluded under any U.S. income tax treaty. For purposes of these rules, §1.706-1(b)(6)(ii) defines a foreign partner as a partner that is not a United States person (as defined in section 7701(a)(30)), but provides that CFCs are not treated as foreign partners. When §1.706-1(b)(6)(ii) was added, CFCs were not treated as foreign partners for purposes of determining a partnership’s taxable year under section 706 because the U.S. owners of such entities were subject to U.S. federal income taxation

on a current basis with respect to certain income earned by these entities. See 66 FR 3920, 3921 (January 17, 2001). As a result of the repeal of section 958(b)(4), a foreign corporation that is a CFC solely by reason of downward attribution from a foreign person may now be taken into account for purposes of determining the taxable year of such partnership. This would include a foreign corporation that is a CFC even if the CFC does not have a U.S. shareholder who owns stock of the foreign corporation within the meaning of section 958(a) and is required to include amounts in income under section 951(a). Accordingly, the proposed regulations exclude from the definition of foreign partner only CFCs with respect to which a U.S. shareholder owns stock within the meaning of section 958(a) for purposes of determining a partnership taxable year. See proposed §1.706-1(b)(6)(ii). As in proposed §1.672(f)-2(a), discussed in Part I.D of this Explanation of Provisions, the reference to foreign personal holding companies is also deleted. See id. The Treasury Department and the IRS request comments on these proposed revisions to §1.706-1(b)(6)(ii).

F. Section 863: Space and ocean income and international communications income of a CFC

Section 863 and the regulations thereunder provide rules for determining the source of certain items of gross income, including gross income from space and ocean activities and international communications income. Section 863(d)(1) provides that, except as provided in regulations, any income derived from a space or ocean activity (“space and ocean income”) by a United States person is sourced in the United States (“U.S. source income”) and that any space and ocean income derived by a foreign person is sourced outside the United States (“foreign source income”). Regulations under section 863(d) include an exception from the statutory provision regarding space

and ocean income derived by a foreign person if the foreign person is a CFC. Specifically, space and ocean income derived by a CFC is treated as U.S. source income, except to the extent that the income, based on all the facts and circumstances, is attributable to functions performed, resources employed, or risks assumed in a foreign country. See §1.863-8(b)(2)(ii).

In the case of any United States person, 50 percent of any international communications income (as defined in section 863(e)(2)) is treated as U.S. source income and 50 percent of such income is treated as foreign source income. Section 863(e)(1)(A). Subject to certain exceptions, including exceptions set forth in regulations, international communications income derived by a foreign person is treated as foreign source income. Section 863(e)(1)(B)(i). Regulations under section 863(e) provide that international communications income derived by a CFC is treated as one-half U.S. source income and one-half foreign source income. See §1.863-9(b)(2)(ii).

The status of the recipient of space and ocean income and international communications income as a CFC solely by reason of the repeal of section 958(b)(4) should not cause all or part of such income to be U.S. source income if it would not have been treated as such otherwise. Accordingly, in accordance with the regulatory authority provided in section 863(d)(1) and (e)(1)(B)(i), and consistent with the temporary relief announced in section 5.01 of Notice 2018-13, 2018-6 I.R.B. 341, these proposed regulations provide that whether a foreign corporation is a CFC for purposes of the rules under sections 863(d) and (e) treating space and ocean income and international communications income as U.S. source income in whole or in part is

determined without regard to downward attribution from a foreign person. See proposed §§1.863-8(b)(2)(ii) and 1.863-9(b)(2)(ii).

G. Section 904: Look-through rules and active rents and royalties exception to categorization as passive category income

In general, section 904(a) limits the amount of foreign income taxes that a taxpayer, including a U.S. shareholder, may claim as a credit against its U.S. income tax based on the taxpayer's foreign source income. Section 904(d) further limits the credit by category of foreign source income, with general category and passive category being two common categories of income. Passive category income includes passive income, which means income that would be FPHCI if the recipient were a CFC. This generally includes dividends, interest, rents, and royalties. See section 904(d)(2)(B)(i) and 954(c)(1)(A). However, if such amounts are received or accrued by a U.S. shareholder of a CFC from the CFC, the amounts are treated as passive category income only to the extent they are allocable to passive category income of the CFC (the "CFC look-through rule"). See section 904(d)(3). Application of the CFC look-through rule requires determining the category of income of the CFC to which the dividends, interest, rents, or royalties paid to the U.S. shareholder (or other related look-through entity) are allocable.

Rents and royalties received by a CFC are generally passive category income unless the income is derived in the active conduct of a trade or business (the "section 904 active rents and royalties exception"), taking into account activities of affiliated group members. See §1.904-4(b)(2)(iii). The section 904 active rents and royalties exception applies both for determining the category to which a U.S. shareholder's inclusion under section 951(a) attributable to the receipt of rents and royalties by a CFC

is assigned under section 904(d)(3)(B), and for purposes of applying the CFC look-through rule to determine the category to which dividends, interest, rents, and royalties paid or accrued by the CFC are allocable under section 904(d)(3)(C) and (D).

Financial services income received by certain CFCs or a domestic corporation is treated as general category income (the “financial services income rule”). See section 904(d)(2)(C)(i). In determining whether income is financial services income for purposes of section 904, the activities of affiliated group members, including CFCs, are taken into account to determine whether such entities are financial services entities (the “financial services entity requirement”). See section 904(d)(2)(C)(ii) and §1.904-4(e)(3)(ii).

The formulation of the CFC look-through rule and the affiliated group rules in both the section 904 active rents and royalties exception and the financial services income rules was premised on the assumption that income of CFCs (including affiliated group members meeting the active conduct requirement or the financial services entity requirement) would be subject to U.S. tax under section 951(a) or on a distribution of earnings and profits generated by such income, and that foreign corporations to which the rules applied would be directly or indirectly controlled by United States persons able to obtain information concerning their activities, income, and expenses. See H.R. Rep. No. 99-841, Volume II, at 566 and 573-574 (1986) (Conf. Rep.); see also T.D. 8412, 57 FR 20639, 20640 (May 14, 1992); id. at 20641; and 66 FR 319, 321 (January 3, 2001). Treating foreign corporations as CFCs or United States persons as U.S. shareholders by reason of downward attribution from foreign persons for purposes of the CFC look-through rule and the affiliated group rules would be inconsistent with the intended scope

of the rules. Before the repeal of section 958(b)(4), a U.S. shareholder of a foreign corporation in which U.S. shareholders held directly or indirectly at least 10 percent, but not more than 50 percent, of the voting stock or value, would be eligible to treat dividends, but not interest, rents, and royalties, as other than passive category income. See section 904(d)(4). Similarly, under the affiliated group rules, neither the active conduct requirement in the section 904 active rents and royalties exception nor the financial services entity requirement in the financial services income rule could be satisfied by a foreign corporation that would be a CFC only by reason of downward attribution from a foreign person.

Accordingly, in accordance with the regulatory authority provided in section 904(d)(7), the regulations under section 904 are revised to limit the application of the affiliated group rules in the section 904 active rents and royalties exception and the financial services income rule, as well as the CFC look-through rule, to foreign corporations that are CFCs without regard to downward attribution from foreign persons. Further, the CFC look-through rule, as proposed to be revised at 83 FR 63200 (December 7, 2018), is further revised to apply only to U.S. shareholders that are U.S. shareholders without regard to downward attribution from foreign persons. See proposed §1.904-5(a)(4)(i) and (vi) (providing definitions that apply for purposes of §§1.904-4 and 1.904-5, pursuant to §§1.904-4(a) and 1.904-5(a)(4) as proposed to be revised at 83 FR 63200 (December 7, 2018)). The Treasury Department and the IRS request comments on these proposed revisions to the regulations under section 904.

H. Section 958: Rules for determining stock ownership

To ensure that the regulations under section 958 are consistent with the amended statute, this notice of proposed rulemaking removes the rule in §1.958-2(d)(2) that corresponds to section 958(b)(4). It also revises Example 4 in §1.958-2(g) to illustrate the application of the ownership attribution rules in section 958 in the absence of section 958(b)(4).

I. Section 1297: PFIC asset test

Section 1297(e) provides the rules used to measure a foreign corporation's assets for purposes of determining whether it meets the asset test in section 1297(a)(2) and is a passive foreign investment company ("PFIC"). If the foreign corporation is a CFC and is not a publicly traded corporation, when determining whether the average percentage of assets of the corporation that produce passive income is at least 50 percent, adjusted basis (rather than value) of the assets must be used. Section 1297(e)(2). Accordingly, shareholders of a foreign corporation that became a CFC as a result of the repeal of section 958(b)(4) will have to determine whether the average percentage of assets that produce passive income is at least 50 percent using adjusted basis.

The legislative history to section 1297(e) indicates that the adjusted basis requirement for CFCs exists because "measurement by adjusted basis is well established in the case of controlled foreign corporations' investments of earnings in U.S. property, and is highly appropriate to the task of measuring the earnings of a controlled foreign corporation that are invested in excess passive assets." H.R. Rep. No. 103-111, at 692 (1993). However, the rule imposes a burden on taxpayers that own stock in foreign corporations that became CFCs solely by reason of the repeal of

section 958(b)(4), which may not otherwise be required to account for the basis in assets under U.S. federal income tax rules. Section 1298(g) grants the Secretary the authority to issue regulations that are necessary and appropriate to carry out the purposes of sections 1291 through 1298. In accordance with this authority, the proposed regulations modify the definition of a CFC for purposes of section 1297(e) to disregard downward attribution from foreign persons. See proposed §1.1297-1(d)(1)(iii)(A).

J. Section 6049: Chapter 61 reporting provisions

Generally, under chapter 61 of subtitle F of the Code, a payor must report to the IRS (using the appropriate Form 1099) certain payments or transactions with respect to United States persons that are not exempt recipients. The regulations under chapter 61 generally provide that the scope of payments or transactions subject to reporting under chapter 61 depends, in part, on whether or not the payor is a U.S. payor (as defined in §1.6049-5(c)(5)), which generally includes United States persons and their foreign branches, as well as CFCs.

Foreign corporations that became CFCs solely as a result of the repeal of section 958(b)(4) could be subject to an increased burden from the reporting requirements under chapter 61 (and the backup withholding rules under section 3406). To mitigate the increased Form 1099 reporting by foreign corporations that may have no direct or indirect owners that are United States persons, in accordance with the regulatory authority provided in section 6049(a), proposed §1.6049-5(c)(5)(i)(C) provides that a U.S. payor includes only a CFC that is a CFC without regard to downward attribution from a foreign person.

II. Applicability Dates

These regulations are generally proposed to apply on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. See section 7805(b)(1)(B). For taxable years before taxable years covered by the regulations, a taxpayer may generally apply the rules set forth in the final regulations to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, and to taxable years of U.S. shareholders in which or with which such taxable years of the foreign corporation end, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply the relevant rule with respect to all foreign corporations. See section 7805(b)(7). Moreover, although proposed §1.958-2 is proposed to apply to taxable years of foreign corporations ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end, the same result as the proposed revisions applies before such date due to the effective date of the repeal of section 958(b)(4).

A taxpayer may rely on the proposed regulations with respect to any period before the date that these regulations are published as final regulations in the **Federal Register**.

Statement of Availability of IRS Documents

IRS Revenue Procedures, Revenue Rulings, notices, and other guidance cited in this document are published in the Internal Revenue Bulletin and are available from the

Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402, or by visiting the IRS website at <http://www.irs.gov>.

Special Analyses

I. Regulatory Planning and Review – Economic Analysis

Executive Orders 13563 and 12866 direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. The Treasury Department requests comment and any potential data regarding the expected impacts of this proposed regulation.

This regulation is subject to review under section 6(b) of Executive Order 12866 pursuant to the April 11, 2018, Memorandum of Agreement (“April 11, 2018 MOA”) between the Treasury Department and the Office of Management and Budget (“OMB”) regarding review of tax regulations. The Acting Administrator of the Office of Information and Regulatory Affairs (“OIRA”), OMB, has waived review of this proposed rule in accordance with section 6(a)(3)(A) of Executive Order 12866. OIRA will subsequently make a significance determination of the final rule under the terms of item 1 of the April 11, 2018 MOA between the Treasury Department and OMB regarding review of tax regulations.

A. Background

Section 14213 of the Act repealed section 958(b)(4), effective beginning with the last taxable year of a foreign corporation that begins before January 1, 2018 (and taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end). The repeal of section 958(b)(4) by the Act modified the constructive ownership rules that determine whether a foreign corporation is a CFC and whether a U.S. person is a U.S. shareholder of a CFC. Under section 318(a)(3), stock owned by a person is attributed downward to (that is, considered to be owned by) a partnership, estate, trust, or corporation in which the person owns an interest. Prior to repeal, section 958(b)(4) limited the application of section 318(a)(3) for purposes of determining whether a foreign corporation is a CFC and whether a U.S. person is a U.S. shareholder by providing that downward attribution under section 318(a)(3) was not applied so as to consider a U.S. person as owning the stock owned by a foreign person. After the repeal of section 958(b)(4), such stock owned by a foreign person can be attributed downward to a U.S. person, for example, to a U.S. subsidiary of a foreign parent. As a result, additional foreign corporations are now CFCs, and U.S. persons are now U.S. shareholders of CFCs, even in cases where the foreign corporation has no or little U.S. ownership.

B. The need for proposed regulations

The legislative history to the Act states that the repeal of section 958(b)(4) was intended “to render ineffective certain transactions that are used to [sic] as a means of avoiding the subpart F provisions.” See H.R. 115-466, at 633 (2017). As a consequence of this repeal, many foreign entities that are part of multinational groups

with U.S. subsidiaries are now considered CFCs even in cases where there is no avoidance of tax under subpart F.

The treatment of a foreign corporation as a CFC, or a U.S. person as a U.S. shareholder, has consequences outside of subpart F because many statutes and regulations outside of subpart F have rules that turn on the status of a foreign corporation as a CFC or the status of a U.S. person as a U.S. shareholder.

These proposed regulations propose changes that are generally intended to ensure that, in appropriate circumstances, the operation of certain rules is consistent with their application before the repeal of section 958(b)(4). This creates continuity and gives taxpayers tax certainty, which allows them to make economically efficient decisions. By restoring the pre-Act rule for certain provisions, the proposed regulations both alleviate certain burdens of CFC status resulting from the section 958(b)(4) repeal unrelated to the aforementioned intended purposes of the repeal and neutralize possible incentives to unfairly exploit the section 958(b)(4) repeal.

C. Baseline

The economic analysis that follows compares the proposed regulations to a no-action baseline reflecting anticipated Federal income tax-related behavior in the absence of the proposed regulations. A no-action baseline reflects the current environment including the existing international tax regulations, prior to any amendment by the proposed regulations.

D. Cost and benefits of the proposed regulations and potential alternatives

As described in Part I.A of this Special Analyses, the repeal of section 958(b)(4) causes stock owned by a foreign parent to be attributed to its U.S. subsidiaries, which

can cause a foreign subsidiary of a foreign parent to be designated as a CFC, even in instances where there is little or no U.S. ownership in the foreign multinational group. The Treasury Department and the IRS estimate the number of U.S. subsidiaries owned 50 percent or more by a foreign corporation to be roughly 75,000 based on 2016 Treasury tax files data. To the extent that these foreign corporations have foreign subsidiaries, they are potentially affected by the proposed regulations. Unfortunately, however, data do not exist regarding the number of such foreign subsidiaries. The costs and benefits of these proposed regulations are discussed further in this Part I.D.

1. Benefits

Restoring continuity with pre-repeal rules in appropriate cases is beneficial in two primary ways. First, it reinstates expected reporting burdens and tax costs for businesses that would otherwise experience unintended and unanticipated increases in these costs due to the unexpected switch to CFC designation described in Part I.A of this Special Analyses. Unanticipated increases in costs can be detrimental to normal business operations and can put affected groups at a disadvantage relative to competitors who did not experience such changes. Regulations designed to maintain continuity of normal business operations are appropriate and will promote a positive business environment relative to the no action baseline.

One of the provisions in these proposed regulations that alleviates burden is the provision under section 863 on income from space and ocean activities and international communications income. In this case (as well as in all other aspects of these proposed regulations), the proposed regulations prevent unintended disruption in business activity by determining CFC status as if section 958(b)(4) had not been

repealed. In the absence of these proposed regulations, foreign-parented multinational groups in the space, ocean, and international communications industries that have U.S. subsidiaries could potentially have their foreign subsidiaries designated as CFCs. The designation of the foreign subsidiaries of the foreign-parented multinational groups as CFCs would result in all (in the case of space and ocean income) or half (in the case of international communications income) of the foreign subsidiary's space and ocean income or international communications income being treated as U.S. source income where the CFCs are controlled directly or indirectly by foreign persons. Comments received suggested that such treatment would render companies' business models untenable. Accordingly, the proposed regulations provide that for purposes of the treatment of space and ocean income and international communications income as U.S. source income, the determination of whether a foreign corporation is a CFC is made without regard to downward attribution from a foreign person. See Part I.F of the Explanation of Provisions for further explanation of this provision.

Another example of reduced burden under this rule relates to the timing of certain transactions. As explained in Part I.A of the Explanation of Provisions, section 267(a)(2) provides a rule for determining the time at which an otherwise deductible amount owed to a related person may be deducted. In general, if a payee is on the cash method of accounting, the payor is not allowed a deduction until the amount is actually paid, even if the payor uses the accrual method of accounting. The current regulations include an exemption that allows an accrual-based payor to deduct certain treaty-exempt amounts before they are actually paid to a related foreign person. However, this exemption is not allowed if the related foreign person is a CFC. Instead,

with respect to an amount owed to a CFC, the payor may only take a deduction in an earlier year to the extent that an amount attributable to the item is includible during such prior taxable year in the gross income of a U.S. person who owns stock in the CFC. However, after the repeal of section 958(b)(4), a CFC may not have any U.S. shareholders that would have an income inclusion under subpart F. In this situation, the payor would be unable to deduct the amount until it is actually paid.

Because of the effective date of the repeal of section 958(b)(4), a foreign corporation that was not a CFC under prior law could now become a CFC beginning as early as January 1, 2017 (even though the Act was not enacted until December 22, 2017). Accordingly, a taxpayer may have deducted an amount accrued in 2017 that, due to the repeal of section 958(b)(4), would no longer be allowable in 2017. Furthermore, due to the reduction of the corporate tax rate in the Act, a deduction allowed on a company's 2017 tax return at the then statutory rate of 35 percent would be valued at 21 percent if the taxpayer were forced to move the deduction to 2018 or 2019. The repeal of section 958(b)(4) in this situation may result in an inadvertent deferral of certain deductions with permanent tax effect and correspondingly create unnecessary required adjustments to the income tax provisions in companies' financial accounting statements. The proposed guidance removes inconsistent annual treatment of deductions for certain treaty-exempt payments in the year the amounts are accrued when the amounts are owed to related foreign corporations that do not have any direct or indirect U.S. shareholders.

The second benefit of restoring pre-Act treatment is that doing so can neutralize unanticipated incentives for tax minimization resulting from the repeal. That is, CFC

status can both increase burdens and offer benefits, but the unintended increase in CFC designations and the ease with which taxpayers can create a CFC could incentivize taxpayers to take advantage of potential benefits arising from CFC status. For example, Part I.B of the Explanation of Provisions describes a proposed revision that is intended to prevent taxpayers from using the special rule for CFCs in section 332(d)(3) to inappropriately avoid U.S. tax on a liquidating distribution. In addition, Part I.D of the Explanation of Provisions describes a proposed revision that is intended to prevent taxpayers from using a CFC that has no direct or indirect U.S. shareholders to take advantage of the special rule relating to CFCs that are grantors of a trust, facilitating tax-free distributions from the trust to U.S. beneficiaries despite no income inclusion by the shareholders of the CFC. Because these benefits were not intended for CFCs without direct or indirect U.S. shareholders, the anti-abuse aspects of these proposed regulations are designed to remove such incentives for taxpayers with those CFCs. Such regulations are beneficial because they promote an environment in which business operations are undertaken based on sound economic principles rather than for tax-motivated reasons.

2. Costs

The proposed regulations restore pre-section 958(b)(4) repeal CFC designation by determining CFC designation in limited situations as if section 958(b)(4) had not been repealed, essentially restoring the pre-repeal “status quo” in these situations. The proposed regulations do not impose any new systems, methods, structures, reporting, or other potentially burdensome rules that could increase compliance costs. In fact, as described above, they reduce costs or burdens that would ensue in the absence of the

proposed regulations. Hence, in restoring the status quo in appropriate circumstances, the proposed regulations are not expected to impose new costs.

II. Regulatory Flexibility Act

It is hereby certified that these proposed regulations will not have a significant economic impact on a substantial number of small entities within the meaning of section 601(6) of the Regulatory Flexibility Act (5 U.S.C. chapter 6). The proposed regulations generally affect CFCs and U.S. shareholders of CFCs. As an initial matter, CFCs, as foreign corporations, are not considered small entities. Nor are U.S. taxpayers considered small entities to the extent the taxpayers are natural persons or entities other than small entities. Thus, the proposed regulations generally only affect small entities if a U.S. taxpayer that is a U.S. shareholder of a CFC is a small entity.

Businesses that are U.S. shareholders of CFCs are generally not small businesses because the ownership of sufficient stock of a CFC in order to be a U.S. shareholder generally entails significant resources and investment. Therefore, the Treasury Department and the IRS have determined that the proposed regulations would not affect a substantial number of domestic small business entities. Moreover, the proposed regulations do not impose any new costs on taxpayers. Consequently, the Treasury Department and the IRS have determined that the proposed regulations will not have a significant economic impact on a substantial number of small entities. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act is not required.

Pursuant to section 7805(f), this notice of proposed rulemaking has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for

comment on its impact on small business. The Treasury Department and the IRS request comments on the impact of these proposed regulations on small business entities.

Comments and Requests for a Public Hearing

Before the proposed regulations are adopted as final regulations, consideration will be given to any comments that are submitted timely to the IRS as prescribed in this preamble under the “ADDRESSES” heading. The Treasury Department and the IRS request comments on all aspects of the proposed regulations. The Treasury Department and the IRS also request comments on whether any other rules should be modified in light of the repeal of section 958(b)(4).

All comments will be available at www.regulations.gov or upon request. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of the proposed regulations are Karen J. Cate and Jorge M. Oben of the Office of Associate Chief Counsel (International). However, other personnel from the Treasury Department and the IRS participated in the development of the proposed regulations.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1--INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by revising the entry for § 1.267(a)-3 and adding entries for §§ 1.332-8 and 1.1297-1 in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.267(a)-3 also issued under 26 U.S.C. 267(a)(3)(A) and (a)(3)(B)(ii).

* * * * *

Section 1.332-8 also issued under 26 U.S.C. 332(d)(4).

* * * * *

Section 1.1297-1 also issued under 26 U.S.C. 1298(g).

* * * * *

Par. 2. Section 1.267(a)-3 is amended by:

1. Removing the language “or (a)(3)” from paragraph (c)(2).
2. Revising paragraph (c)(4).
3. In paragraph (d), revising the second sentence and adding five sentences at the end of the paragraph.

The revisions and addition read as follows:

§1.267(a)-3 Deduction of amounts owed to related foreign persons.

* * * * *

(c) * * *

(4) Certain amounts owed to certain controlled foreign corporations. An amount (other than interest) that is income of a related foreign person with respect to which the related foreign person is exempt from United States taxation on the amount owed

pursuant to a treaty obligation of the United States (such as under an article relating to the taxation of business profits) is exempt from the application of section 267(a)(3)(B)(i) if the related foreign person is a controlled foreign corporation that does not have any United States shareholders (as defined in section 951(b)) that own (within the meaning of section 958(a)) stock of the controlled foreign corporation.

* * * * *

(d) * * * Except as otherwise provided in this paragraph (d), the regulations in this section issued under section 267 apply to all other deductible amounts that are incurred after July 31, 1989, but do not apply to amounts that are incurred pursuant to a contract that was binding on September 29, 1983, and at all times thereafter (unless the contract was renegotiated, extended, renewed, or revised after that date). Paragraph (c)(2) of this section applies to payments accrued on or after October 22, 2004. For payments accrued before October 22, 2004, see §1.267(a)-3(c)(2), as contained in 26 CFR part 1, revised as of April 1, 2004. Paragraph (c)(4) of this section applies to payments accrued on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For payments accrued before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, a taxpayer may apply paragraph (c)(4) of this section for payments accrued during the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such paragraph with respect to all foreign corporations. For payments accrued before October 22, 2004, see §1.267(a)-3(c)(4), as contained in 26 CFR part 1, revised as of April 1, 2004.

Par. 3. Section 1.332-8 is added to read as follows:

§1.332-8 Recognition of gain on liquidation of certain holding companies.

(a) Definition of controlled foreign corporation. For purposes of section 332(d)(3), a controlled foreign corporation has the meaning provided in section 957, determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

(b) Applicability date. This section applies to distributions in complete liquidation occurring on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and to distributions in complete liquidation occurring before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, that result from an entity classification election made under §301.7701-3 of this chapter that is filed on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For distributions in complete liquidation occurring before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, other than distributions in complete liquidation occurring before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, that result from an entity classification election made under §301.7701-3 of this chapter that is filed on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, a taxpayer may apply this section to distributions in complete liquidation occurring during the last taxable year of a distributee foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply this section with respect to all foreign corporations.

Par. 4. Section 1.367(a)-8 is amended by:

1. Revising the second sentence of paragraph (k)(14)(ii).
2. In paragraph (p)(3), designating Examples 1 through 3 as paragraphs (p)(3)(i) through (iii), respectively.
3. In newly redesignated paragraphs (p)(3)(i) through (iii), redesignating the paragraphs in the first column as the paragraphs in the second column:

Old Paragraphs	New Paragraphs
(p)(3)(i)(i) and (ii)	(p)(3)(i)(A) and (B)
(p)(3)(ii)(i) and (ii)	(p)(3)(ii)(A) and (B)
(p)(3)(iii)(i) and (ii)	(p)(3)(iii)(A) and (B)

4. In each newly redesignated paragraph listed in the first column, removing the language in the second column and adding in its place the language in the third column:

Paragraph	Remove	Add
(p)(3)(i)(B)	this <u>Example 1</u>	In paragraph (p)(3)(i)(A) of this section (the facts of this <u>Example 1</u>)
(p)(3)(ii)(B)	this <u>Example 2</u>	In paragraph (p)(3)(ii)(A) of this section (the facts of this <u>Example 1</u>)

5. In paragraph (q)(2):

a. Removing the language “at least 5% (applying the attribution rules of section 318, as modified by section 958(b))” each place that it appears and adding “at least 5% (determined as provided in paragraph (k)(14)(ii) of this section)” in its place.

b. Designating Examples 1 through 25 as paragraphs (q)(2)(i) through (xxv), respectively.

6. In newly redesignated paragraphs (q)(2)(i) through (xxv), redesignating the paragraphs in the first column as the paragraphs in the second column:

Old Paragraphs	New Paragraphs
(q)(2)(i)(i) and (ii)	(q)(2)(i)(A) and (B)
(q)(2)(ii)(i) and (ii)	(q)(2)(ii)(A) and (B)
(q)(2)(ii)(B)(A) and (B)	(q)(2)(ii)(B)(<u>1</u>) and (<u>2</u>)
(q)(2)(iii)(i) and (ii)	(q)(2)(iii)(A) and (B)
(q)(2)(iv)(i) and (ii)	(q)(2)(iv)(A) and (B)
(q)(2)(iv)(B)(A) and (B)	(q)(2)(iv)(B)(<u>1</u>) and (<u>2</u>)
(q)(2)(iv)(B)(<u>2</u>)(<u>1</u>) through (<u>3</u>)	(q)(2)(iv)(B)(<u>2</u>)(i) through (<u>iii</u>)
(q)(2)(v)(i) and (ii)	(q)(2)(v)(A) and (B)
(q)(2)(vi)(i) through (iii)	(q)(2)(vi)(A) through (C)
(q)(2)(vi)(B)(A) and (B)	(q)(2)(vi)(B)(<u>1</u>) and (<u>2</u>)
(q)(2)(vi)(B)(<u>2</u>)(<u>1</u>) through (<u>3</u>)	(q)(2)(vi)(B)(<u>2</u>)(i) through (<u>iii</u>)
(q)(2)(vii)(i) and (ii)	(q)(2)(vii)(A) and (B)
(q)(2)(viii)(i) and (ii)	(q)(2)(viii)(A) and (B)
(q)(2)(ix)(i) and (ii)	(q)(2)(ix)(A) and (B)
(q)(2)(x)(i) and (ii)	(q)(2)(x)(A) and (B)

(q)(2)(x)(B)(A) through (C)	(q)(2)(x)(B)(<u>1</u>) through (<u>3</u>)
(q)(2)(xi)(i) through (iii)	(q)(2)(xi)(A) through (C)
(q)(2)(xii)(i) and (ii)	(q)(2)(xii)(A) and (B)
(q)(2)(xii)(B)(A) through (C)	(q)(2)(xii)(B)(<u>1</u>) through (<u>3</u>)
(q)(2)(xiii)(i) and (ii)	(q)(2)(xiii)(A) and (B)
(q)(2)(xiv)(i) and (ii)	(q)(2)(xiv)(A) and (B)
(q)(2)(xiv)(B)(A) and (B)	(q)(2)(xiv)(B)(<u>1</u>) and (<u>2</u>)
(q)(2)(xv)(i) and (ii)	(q)(2)(xv)(A) and (B)
(q)(2)(xvi)(i) and (ii)	(q)(2)(xvi)(A) and (B)
(q)(2)(xvii)(i) and (ii)	(q)(2)(xvii)(A) and (B)
(q)(2)(xvii)(B)(A) through (C)	(q)(2)(xvii)(B)(<u>1</u>) through (<u>3</u>)
(q)(2)(xvii)(B)(<u>3</u>)(<u>1</u>) through (<u>3</u>)	(q)(2)(xvii)(B)(<u>3</u>)(i) through (<u>iii</u>)
(q)(2)(xviii)(i) and (ii)	(q)(2)(xviii)(A) and (B)
(q)(2)(xix)(i) and (ii)	(q)(2)(xix)(A) and (B)
(q)(2)(xx)(i) through (vi)	(q)(2)(xx)(A) through (F)
(q)(2)(xx)(B)(A) and (B)	(q)(2)(xx)(B)(<u>1</u>) and (<u>2</u>)
(q)(2)(xx)(B)(<u>1</u>)(<u>1</u>) and (<u>2</u>)	(q)(2)(xx)(B)(<u>1</u>)(i) and (<u>ii</u>)
(q)(2)(xxi)(i) and (ii)	(q)(2)(xxi)(A) and (B)
(q)(2)(xxi)(B)(A) through (C)	(q)(2)(xxi)(B)(<u>1</u>) through (<u>3</u>)
(q)(2)(xxii)(i) through (iii)	(q)(2)(xxii)(A) through (C)
(q)(2)(xxii)(B)(A) through (C)	(q)(2)(xxii)(B)(<u>1</u>) through (<u>3</u>)
(q)(2)(xxii)(C)(A) through (C)	(q)(2)(xxii)(C)(<u>1</u>) through (<u>3</u>)
(q)(2)(xxiii)(i) through (iv)	(q)(2)(xxiii)(A) through (D)

(q)(2)(xxiii)(B)(A) through (D)	(q)(2)(xxiii)(B)(<u>1</u>) through (<u>4</u>)
(q)(2)(xxiii)(C)(A) and (B)	(q)(2)(xxiii)(C)(<u>1</u>) and (<u>2</u>)
(q)(2)(xxiv)(i) and (ii)	(q)(2)(xxiv)(A) and (B)
(q)(2)(xxv)(i) and (ii)	(q)(2)(xxv)(A) and (B)

7. In each newly redesignated paragraph listed in the first column, removing the language in the second column and adding in its place the language in the third column:

Paragraph	Remove	Add
(q)(2)(ii)(B)(<u>2</u>)	paragraph (ii)(A) of this <u>Example 2</u>	paragraph (q)(2)(ii)(B)(<u>1</u>) of this section (paragraph (<u>1</u>) in the results in this <u>Example 2</u>)
(q)(2)(iv)(B)(<u>2</u>)(i)	paragraph (ii)(A) of this <u>Example 4</u>	paragraph (q)(2)(iv)(B)(<u>1</u>) of this section (paragraph (<u>1</u>) in the results in this <u>Example 4</u>)
(q)(2)(vi)(B)(<u>1</u>)	paragraph (ii)(B) of this <u>Example 6</u>	paragraph (q)(2)(vi)(B)(<u>2</u>) of this section (paragraph (<u>2</u>) in the results in this <u>Example 6</u>)
(q)(2)(vi)(C)	paragraph (i) of this <u>Example 6</u>	paragraph (q)(2)(vi)(A) of this section (the facts in this <u>Example 6</u>)

(q)(2)(xi)(C)	paragraph (i) of this <u>Example 11</u>	paragraph (q)(2)(xi)(A) of this section (the facts in this <u>Example 11</u>)
(q)(2)(xx)(C)	paragraph (i) of this <u>Example 20</u>	paragraph (q)(2)(xx)(A) of this section (the facts in this <u>Example 20</u>)
(q)(2)(xx)(C)	paragraph (ii) of this <u>Example 20</u>	paragraph (q)(2)(xx)(B) of this section (the results in this <u>Example 20</u>)
(q)(2)(xx)(D)	paragraph (i) of this <u>Example 20</u>	paragraph (q)(2)(xx)(A) of this section (the facts in this <u>Example 20</u>)
(q)(2)(xx)(D)	paragraph (ii) of this <u>Example 20</u>	paragraph (q)(2)(xx)(B) of this section (the facts in this <u>Example 20</u>)
(q)(2)(xx)(E)	paragraph (i) of this <u>Example 20</u>	paragraph (q)(2)(xx)(A) of this section (the facts in this <u>Example 20</u>)
(q)(2)(xx)(F)	paragraph (i) of this <u>Example 20</u>	paragraph (q)(2)(xx)(A) of this section (the facts in this <u>Example 20</u>)
(q)(2)(xxii)(C) introductory text	in paragraph (i) of this <u>Example 22</u>	paragraph (q)(2)(xxii)(A) of this section (the facts in this

		<u>Example 22)</u>
(q)(2)(xxiii)(C) introductory text	paragraph (i) of this <u>Example 23</u>	paragraph (q)(2)(xxiii)(A) of this section (the facts in this <u>Example 23</u>)
(q)(2)(xxiii)(C) introductory text	paragraph (ii) of this <u>Example 23</u>	paragraph (q)(2)(xxiii)(B) of this section (the results in this <u>Example 23</u>)
(q)(2)(xxiii)(D)	paragraph (i) of this <u>Example 23</u>	paragraph (q)(2)(xxiii)(A) of this section (the facts in this <u>Example 23</u>)
(q)(2)(xxiv)(A)	in paragraph (i) of <u>Example 6</u>	paragraph (q)(2)(vi)(A) of this section (the facts in <u>Example 6</u>)

8. Amend each paragraph listed in the first column, by removing the language in the second column and adding in its place the language in the third column:

Paragraph	Remove	Add
(c)(1)(ii)	(q)(2) of this section, Example 6	(q)(2)(vi) of this section
(c)(4)(iv)	paragraph (q)(2) of this section, Examples 1, 2, 3, and 5	paragraphs (q)(2)(i), (ii), (iii), and (v) of this section
(j)(1)	(q)(2) of this section,	(q)(2)(ii) of this section

	Example 2	
(k)(1) introductory language	(q)(2) of this section, Example 4	(q)(2)(iv) of this section
(k)(1)(ii)	(q)(2) of this section, Example 3	(q)(2)(iii) of this section
(k)(1)(iii)	(q)(2) of this section, Example 11	(q)(2)(xi) of this section
(k)(6)(i)	(q)(2) of this section, Example 5	(q)(2)(v) of this section
(k)(6)(i)	(q)(2) of this section, Example 6	(q)(2)(vi) of this section
(k)(6)(ii)	(q)(2) of this section, Example 7	(q)(2)(vii) of this section
(k)(6)(iii)	(q)(2) of this section, Example 8	(q)(2)(viii) of this section
(k)(8)	(q)(2) of this section, Example 9	(q)(2)(ix) of this section
(k)(12)(i)	(q)(2) of this section, Example 20	(q)(2)(xx) of this section
(k)(14) introductory language	paragraph (q)(2), Examples 4, 6, 10, 12, 17, 21, and 23 of this section	paragraphs (q)(2)(iv), (vi), (x), (xii), (xvii), (xxi), and (xxiii) of this section
(m)(1)	(q)(2) of this section,	(q)(2)(xiii) of this section

	Example 13	
(n)(1)	(q)(2) of this section, Example 14	(q)(2)(xiv) of this section
(o)(1)(ii)	(q)(2) of this section, Example 15	(q)(2)(xv) of this section
(o)(1)(iii) introductory language	(q)(2) of this section, Example 16	(q)(2)(xvi) of this section
(o)(5)(i)(A)	(q)(2) of this section, Example 18	(q)(2)(xviii) of this section
(o)(5)(i)(B)	(q)(2) of this section, Example 19	(q)(2)(ixx) of this section
(o)(5)(i)(C)	(q)(2) of this section, Example 22	(q)(2)(xxii) of this section
(o)(5)(i)(D)	(q)(2) of this section, Example 22	(q)(2)(xxii) of this section
(o)(6)	(q)(2) of this section, Example 20	(q)(2)(xx) of this section
(r)(2)(i)	paragraph (q)(2) of this section, Examples 24 and 25	paragraphs (q)(2)(xxiv) and (xxv) of this section

9. Revising the heading of paragraph (r).

10. Adding two sentences at the end of paragraph (r)(1)(i).

The revision and addition read as follows:

§1.367(a)-8 Gain recognition agreement requirements.

* * * * *

(k) * * *

(14) * * *

(ii) * * * If, as a result of the disposition or other event, a foreign corporation acquires the transferred stock or securities or, as applicable, substantially all the assets of the transferred corporation, the condition of this paragraph (k)(14)(ii) is satisfied only if the U.S. transferor owns at least five percent (applying the attribution rules of section 318, as modified by section 958(b), without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider the U.S. transferor as owning stock which is owned by a person who is not a United States person) of the total voting power and the total value of the outstanding stock of such foreign corporation.

* * * * *

(r) Applicability dates. (1) * * *

(i) * * * Paragraph (k)(14)(ii) of this section applies to transfers occurring on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and to transfers occurring before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, that result from an entity classification election made under §301.7701-3 of this chapter that is filed on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For transfers occurring before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, other than transfers occurring before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, that result from an entity classification election made under §301.7701-3

of this chapter that is filed on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, a taxpayer may apply paragraph (k)(14)(ii) of this section to transfers occurring during the last taxable year of a transferee foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such paragraph with respect to all foreign corporations.

* * * * *

Par. 5. Section 1.672(f)-2 is amended by revising paragraphs (a) and (e) to read as follows:

§1.672(f)-2 Certain foreign corporations.

(a) Application of general rule in this section. Subject to the provisions of paragraph (b) of this section, if the owner of any portion of a trust upon application of the grantor trust rules without regard to section 672(f) is a controlled foreign corporation or a passive foreign investment company (as defined in section 1297), the corporation will be treated as a domestic corporation for purposes of applying the rules of §1.672(f)-1. For purposes of this section, the only controlled foreign corporations taken into account are those that are controlled foreign corporations within the meaning provided in section 957, determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

* * * * *

(e) Applicability dates. Except as provided in this paragraph (e), the rules of this section apply to taxable years of shareholders of controlled foreign corporations and passive foreign investment companies beginning after August 10, 1999, and taxable years of controlled foreign corporations and passive foreign investment companies ending with or within such taxable years of the shareholders. The provisions in paragraph (a) of this section relating to the controlled foreign corporations taken into account for purposes of this section apply to taxable years of foreign corporations ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and taxable years of United States shareholders in which or with which such taxable years of foreign corporations end. For taxable years of foreign corporations ending before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and taxable years of United States shareholders in which or with which such taxable years of foreign corporations end, a taxpayer may apply such provisions to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, and to taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such provisions with respect to all foreign corporations.

Par. 6. Section 1.706-1 is amended by:

1. Revising paragraph (b)(6)(ii).
2. Revising the heading for paragraph (b)(6)(v).

3. In paragraph (b)(6)(v)(A), revising the first sentence and adding two sentences after the first sentence.

The revisions and addition read as follows:

§1.706-1 Taxable years of partner and partnership.

* * * * *

(b) * * *

(6) * * *

(ii) Definition of foreign partner. For purposes of this paragraph (b)(6), a foreign partner is any partner that is not a United States person (as defined in section 7701(a)(30)), except that a partner that is a controlled foreign corporation (within the meaning of section 957(a)) in which a United States shareholder (as defined in section 951(b)) owns (within the meaning of section 958(a)) stock is not treated as a foreign partner.

* * * * *

(v) Applicability dates. (A) * * * The provisions of this paragraph (b)(6) (other than paragraph (b)(6)(iii) of this section and paragraph (b)(6)(ii) of this section to the extent described in the next sentence) apply to partnership taxable years, other than those of an existing partnership, that begin on or after July 23, 2002. The provisions in paragraph (b)(6)(ii) of this section relating to controlled foreign corporations apply to taxable years of foreign corporations ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and taxable years of United States shareholders in which or with which such taxable years of foreign corporations end. For taxable years of foreign corporations ending before **[INSERT DATE OF FILING IN THE FEDERAL**

REGISTER], and taxable years of United States shareholders in which or with which such taxable years of foreign corporations end, a taxpayer may apply such provisions to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, and to taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such provisions with respect to all foreign corporations. * * *

* * * * *

Par. 7. Section 1.863-8 is amended by:

1. In paragraph (b)(2)(ii), revising the first sentence and adding a sentence at the end of the paragraph.
2. Revising paragraph (h).

The revisions and addition read as follows:

§1.863-8 Source of income derived from space and ocean activity under section 863(d).

* * * * *

(b) * * *

(2) * * *

(ii) * * * Space and ocean income derived by a controlled foreign corporation (CFC) is income from sources within the United States. * * * For purposes of this section, a controlled foreign corporation has the meaning provided in section 957, determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as

to consider a United States person as owning stock which is owned by a person who is not a United States person.

* * * * *

(h) Applicability dates. Except as provided in this paragraph (h), this section applies to taxable years beginning on or after December 27, 2006. The provisions in paragraph (b)(2)(ii) of this section relating to the meaning of CFC apply to taxable years of foreign corporations ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For taxable years of foreign corporations ending before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, a taxpayer may apply such provisions to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such provisions with respect to all foreign corporations.

Par. 8. Section 1.863-9 is amended by revising paragraphs (b)(2)(ii) and (l) to read as follows:

§1.863-9 Source of income derived from communications activity under section 863(a), (d), and (e).

* * * * *

(b) * * *

(2) * * *

(ii) International communications income derived by a controlled foreign corporation. International communications income derived by a controlled foreign corporation (CFC) is one-half from sources within the United States and one-half from

sources without the United States. For purposes of this section, a controlled foreign corporation has the meaning provided in section 957, determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

* * * * *

(l) Applicability dates. Except as otherwise provided in this paragraph (l), this section applies to taxable years beginning on or after December 27, 2006. The provisions in paragraph (b)(2)(ii) of this section relating to the meaning of CFC apply to taxable years of foreign corporations ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For taxable years of foreign corporations ending before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, a taxpayer may apply such provisions to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such provisions with respect to all foreign corporations.

Par. 9. Section 1.904-5, as proposed to be amended at 83 FR 63200 (December 7, 2018), is further amended by:

1. Revising paragraph (a)(4)(i).
2. Revising the first sentence of paragraph (a)(4)(vi).
3. Revising paragraph (o).

The revisions read as follows:

§1.904-5 Look-through rules as applied to controlled foreign corporations and other entities.

(a) * * *

(4) * * *

(i) The term controlled foreign corporation has the meaning given such term by section 957 (taking into account the special rule for certain captive insurance companies contained in section 953(c)), determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

* * * * *

(vi) The term United States shareholder has the meaning given such term by section 951(b) (taking into account the special rule for certain captive insurance companies contained in section 953(c)), determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider a United States person as owning stock which is owned by a person who is not a United States person, except that for purposes of this section, a United States shareholder includes any member of the controlled group of the United States shareholder. * * *

* * * * *

(o) Applicability dates. Except as otherwise provided in this paragraph (o), this section applies to taxable years that both begin after December 31, 2017, and end on or after December 4, 2018. Paragraphs (a)(4)(i) and (vi) of this section apply to taxable years of foreign corporations ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and taxable years of United States persons ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For taxable years of foreign corporations ending before **[INSERT DATE OF FILING IN THE FEDERAL**

REGISTER], and taxable years of United States persons ending before **INSERT DATE**
OF FILING IN THE FEDERAL REGISTER], a taxpayer may apply such provisions to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, and to taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such provisions with respect to all foreign corporations.

Par. 10. Section 1.958-2 is amended by:

1. Removing and reserving paragraph (d)(2).
2. In paragraph (g), designating Examples 1 through 6 as paragraphs (g)(1) through (6), respectively.
3. In newly designated paragraphs (g)(1) and (2), removing the language “paragraph (c)(1)(iii) and (2) of this section” and adding “paragraphs (c)(1)(iii) and (c)(2) of this section” in its place.
4. Revising newly designated paragraph (g)(4).
5. Adding paragraph (h).
6. Removing the parenthetical authority citation at the end of the section.

The revisions and addition read as follows:

§1.958-2 Constructive ownership of stock.

* * * * *

(g) * * *

(4) Example 4. Foreign corporation U owns 100 percent of the one class of stock in domestic corporation V and also 100 percent of the one class of stock in foreign

corporation W. Because more than 50 percent in value of the stock of V Corporation is owned by its sole shareholder, U Corporation, V Corporation is considered under paragraph (d)(1)(iii) of this section as owning the stock owned by U Corporation in W Corporation, and accordingly is a United States shareholder of W Corporation.

* * * * *

(h) Applicability date. Paragraphs (d)(2) and (g)(4) of this section apply to taxable years of foreign corporations ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and taxable years of United States shareholders in which or with which such taxable years of foreign corporations end. For taxable years of foreign corporations ending before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, and taxable years of United States shareholders in which or with which such taxable years of foreign corporations end, a taxpayer may apply such provisions to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, and to taxable years of United States shareholders in which or with which such taxable years of the foreign corporation end, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such provisions with respect to all foreign corporations.

Par. 11. Section 1.1297-1, as proposed to be added at 84 FR 33120 (July 11, 2019), is amended by revising paragraphs (d)(1)(iii)(A) and (g)(1) to read as follows:

§1.1297-1 Definition of passive foreign investment company.

* * * * *

(d) * * *

(1) * * *

(A) Controlled foreign corporation. For purposes of section 1297(e)(2)(A), the term controlled foreign corporation has the meaning provided in section 957, determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

* * * * *

(g) * * *

(1) Paragraph (d)(1)(iii)(A) of this section. Paragraph (d)(1)(iii)(A) of this section applies to taxable years of shareholders ending on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For taxable years of shareholders ending before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, a shareholder may apply paragraph (d)(1)(iii)(A) of this section to the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the shareholder and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such paragraph with respect to all foreign corporations.

* * * * *

Par. 12. Section 1.6049-5 is amended by revising paragraphs (c)(5)(i)(C) and (g) to read as follows:

§1.6049-5 Interest and original issue discount subject to reporting after December 31, 1982.

* * * * *

(c) * * *

(5) * * *

(i) * * *

(C) A controlled foreign corporation within the meaning of section 957, determined without applying subparagraphs (A), (B), and (C) of section 318(a)(3) so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

* * * * *

(g) Applicability dates. Except as otherwise provided in this paragraph (g), this section applies to payments made on or after January 6, 2017. (For payments made after June 30, 2014, and before January 6, 2017, see this section as in effect and contained in 26 CFR part 1, as revised April 1, 2016. For payments made after December 31, 2000, and before July 1, 2014, see this section as in effect and contained in 26 CFR part 1, as revised April 1, 2013.) Paragraph (c)(5)(i)(C) of this section applies to payments made on or after **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**. For payments made before **[INSERT DATE OF FILING IN THE FEDERAL REGISTER]**, a taxpayer may apply paragraph (c)(5)(i)(C) of this section for payments during the last taxable year of a foreign corporation beginning before January 1, 2018, and each subsequent taxable year of the foreign corporation, provided that the taxpayer and United States persons that are related (within the meaning of section 267 or 707) to the taxpayer consistently apply such paragraph with respect to all foreign corporations.

Kirsten Wielobob,

Deputy Commissioner for Services and Enforcement.